Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Briggs	Analyst:	Roger Lackey	Bill Number:	AB 641
Related Bills:	See Legislative History	Telephone:	845-3627	Introduced Date:	04-16-2001
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Targeted Tax Area/Approve Expansion Of No More Than 15%

SUMMARY

This bill would:

- Expand a Targeted Tax Area (TTA) by no more than 15%.
- Add agricultural services and business services to the list of trades or businesses that may claim TTA tax incentives.
- Amend the TTA hiring credit to reference the Workforce Investment Act of 1998.

This analysis will not address the bill's provision regarding government contracts that would be performed within a TTA.

SUMMARY OF AMENDMENTS

The April 16, 2001, amendment made the following changes:

- Removed two of the conditions that would have been required to expand a TTA by 15%.
- Added taxpayers engaged in business services to the list of taxpayers that would be eligible for the tax incentives allowed in a TTA.
- Added an election related to limits on tax incentives based on business income apportioned to a TTA.
- Deleted language in the TTA sales or use tax credit that allows only one income tax credit to be claimed on the qualified property.
- Added new provisions regarding government contracts.

This is the department's first analysis of the bill.

PURPOSE OF THE BILL

The author's staff has indicated the purpose of the bill is to expand the TTA benefits to additional areas and services.

Board Position:			Department Director	Date
______ S	______ NA	______ NP	Alan Hunter for GHG	05/02/01
______ SA	______ O	______ NAR		
______ N	______ OUA	__X__ PENDING		

EFFECTIVE/OPERATIVE DATE

This bill is a tax levy and would be effective upon enactment. It would apply to taxable years beginning on or after January 1, 2001.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Federal law does not have TTAs; however, federal law does provide for other economic development areas, such as empowerment zones and enterprise communities.

Under the Government Code, existing state law allows for the designation of a TTA. Using specified criteria regarding unemployment, income levels, poverty levels, and percentages of residents receiving Aid to Families with Dependent Children, TCA designated Tulare County as a TTA. This TTA was designated November 1, 1998, and the designation is binding for 15 years beginning January 1, 1998.

Under the Revenue and Taxation Code, state law allows special tax incentives for taxpayers conducting business activities within the TTA. These incentives include a sales or use tax credit, hiring credit, business expense deduction, and special net operating loss treatment.

THIS BILL

This bill would require TCA to approve expansion of the TTA by no more than 15%, if the increased area meets the necessary criteria to be a TTA (unemployment, income levels, poverty levels, and percentages of people receiving Aid to Families with Dependent Children, based on 1995-96 numbers). It would also require the governing body of each city, county, and city and county in which the TTA is located to approve an ordinance or resolution approving the proposed expansion.

For purposes of the TTA, this bill also would amend existing law to add agricultural services and business services to the list of trades or businesses that may claim the tax incentives available in a TTA.

- Agricultural services would include soil preparation, crop planting and harvesting, veterinary, livestock and animal services, farm labor and management, and landscape and horticultural services.

- Business services would include advertising, consumer credit reporting agencies, mercantile reporting agencies, adjustment and collection agencies, mailing, reproduction, commercial art and photography, and stenographic services, services to dwellings and other buildings, miscellaneous equipment rental and leasing, personnel supply services, computer programming data processing, and other computer related services, and miscellaneous business services.

For purposes of the tax incentives available in a TTA, this bill would allow an election to a taxpayer whose business income apportioned to the TTA is less than 25% of the taxpayer's total business income attributable to sources in this state. The taxpayer would be allowed to elect the greater of the amount of business income apportioned to the TTA or 25% of the business income attributable to sources in this state.

For the hiring credit, this bill would delete the reference to the federal "Job Training Partnership Act," and substitute a reference to the "Workforce Investment Act of 1998." It also would correct a subdivision reference regarding the principles that apply to controlled groups with respect to determining employment.

For the sales or use tax credit, this bill would delete the limitation that a taxpayer can only claim one income tax credit for the qualified property.

IMPLEMENTATION CONSIDERATIONS

Use of the word "elect" denotes that a taxpayer must make an irrevocable election on the original return and cannot deviate from that election absent consent of the FTB. However, this bill would not provide FTB that authority. The author should make sure that the taxpayer is aware that an election is irrevocable and that if a taxpayer has an adjustment to factors at a later date that may increase the TTA percentage over 25%, they could not change the election to obtain the higher amount.

It is not clear how the 25% business income attributable to sources in the state would be calculated and apportioned. If the author intends that the business income be apportioned using the general apportioning rules, the author may consider referencing those rules in the provision.

After resolution of the concern relating to the apportionment provision, implementation of this bill would not significantly impact the department's programs and operations.

TECHNICAL CONSIDERATIONS

Under the Personal Income Tax Law, this bill would amend the sales or use tax credit to insert "including but not limited to" in lieu of "such as" in several places. However, these changes are not made to the credit under the Bank and Corporation Tax Law. These technical changes should be made to both credits for consistency.

This bill would amend a technical error in the TTA NOL statute. The bill would simply redesignate the subdivision reference to correct the erroneous labeling of two subdivisions as subdivision (b). As a result, it was also necessary to make corresponding changes to other subdivision references.

However, the change made to one subdivision reference was incorrect. Amendment 1 would resolve the incorrect reference.

LEGISLATIVE HISTORY

AB 2090 (Reyes, 1999/2000) would have expanded a TTA by up to 15%, and would have added certain crop preparation services to the list of trades or businesses that may claim the tax incentives applicable in a TTA. This bill died in Assembly Appropriations.

OTHER STATES' INFORMATION

Currently, 29 other states have economic development areas that provide similar tax related incentives as those provided by California's economic development areas. The number of economic development areas varies from state to state. For example, *California* currently has 50 economic development areas, while *New York* has 58; *Florida*, 32; *Illinois*, 93; and *Michigan*, 23.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

Tax Revenue Estimate

Based on data and assumptions discussed below, revenue impact of this proposal is projected to be as follows:

Estimated Revenue Impact of **AB 641** As Amended April 16, 2001 For Taxable/Income Years After 12/31/2000			
Fiscal Years	2001/02	2002/03	2003/04
Revenue Impact	**($0.5)**	**($1)**	**($1.5)**

Any possible changes in employment, personal income, or gross state product that might result from this provision are not taken into account.

Revenue Discussion

Revenue losses would primarily depend on the number of businesses in the extended targeted tax area that would purchase qualified property (subject to the sales tax), the amount of wages paid to qualified employees, and the relevant state tax liabilities of employers claiming these tax benefits.

According to departmental data for tax year 1999, there were nearly $685,000 of approved tax credits reported for eight existing targeted tax areas (an average of $85,000 per area). This bill would expand eligible businesses to all tax targeted areas and potential geographical borders to certain areas.

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO AB 641
As Amended April 16, 2001

AMENDMENT 1

On page 24, line 2, strikeout "(e)" and insert:

(d)